

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
A COMPONENT UNIT OF THE STATE OF WEST VIRGINIA AND  
WEST VIRGINIA DEPARTMENT OF TRANSPORTATION

AUDITED FINANCIAL STATEMENTS  
WITH ADDITIONAL INFORMATION

YEAR ENDED JUNE 30, 2003  
AND  
INDEPENDENT AUDITORS' REPORTS

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## INDEPENDENT AUDITORS' REPORT

Joint Committee on Government and Finance  
West Virginia Legislature

We have audited the accompanying financial statements of the governmental activities and each major fund, of the West Virginia Department of Transportation, Division of Highways, as of and for the year ended June 30, 2003, as listed in the table of contents. These financial statements are the responsibility of the West Virginia Department of Transportation, Division of Highways' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements of the West Virginia Department of Transportation, Division of Highways are intended to present the financial position and the changes in financial position of only that portion of the governmental activities and each major fund of the West Virginia Department of Transportation and of the State of West Virginia, that is attributable to the transactions of the Division of Highways. They do not purport to, and do not, present fairly, the financial position of the West Virginia Department of Transportation or the State of West Virginia as of June 30, 2003 and the changes in their financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the West Virginia Department of Transportation, Division of Highways, as of June 30, 2003, and the respective changes in financial position thereof and the respective budgetary comparison for the State Road (General) Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 5 through 15 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 31, 2003 on our consideration of the West Virginia Department of Transportation, Division of Highways' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

*Suttle & Stalnaker, PLLC*

October 31, 2003

MANAGEMENT'S DISCUSSION AND ANALYSIS

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
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This section of the West Virginia Department of Transportation, Division of Highways (Division) annual financial report presents our discussion and analysis of the Division's financial performance during the fiscal year that ended June 30, 2003. This section introduces the basic financial statements and provides an analytical overview of the Division's financial activities. Please read it in conjunction with the Division's financial statements, which immediately follow this section.

During the current year it was determined that an undercapitalization of infrastructure assets had occurred in the initial implementation of the provisions of GASB Statement 34 *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. Certain projects that met the capitalization criteria were excluded from Work in Progress and other projects that were completed were not properly capitalized into infrastructure. This undercapitalization of infrastructure assets affected only the government-wide financial statements. There was no impact on the fund or budgetary comparison financial statements for the year ended June 30, 2002. Applicable prior year amounts included in this section reflect the restated amounts.

### FINANCIAL HIGHLIGHTS - PRIMARY GOVERNMENT

*Net Assets* - The Division's total combined net assets increased by \$235 million, 4.20%, between fiscal year 2002 and 2003.

*Changes in Net Assets* - During the year the Division's expenses were \$235 million less than the \$988 million generated in revenues for governmental activities. This is an improvement over the prior year, when expenses were \$227 million less than revenues.

*Revenues and Expenses* - Total revenues decreased by \$45 million or 4.43%. Total expenses decreased \$54 million or 6.65%. There were no significant changes in the programs carried out by the Division during the year.

*Governmental Funds - Fund Balances* - As of the close of fiscal year 2003, the Division's governmental funds reported combined total fund equity of \$203 million, a decrease of \$44 million in comparison with the prior year. Of this total amount, \$144 million represents the "unreserved fund balances" with substantially all being in the general fund. This is approximately 13.14 % of the total governmental fund expenditures for the year.

*Long-term Debt* - The Division's total long-term debt obligations, net of bond premiums, decreased by \$23 million (4.21%) during the current fiscal year. There were no new bond offerings during the year and principal payments reduced outstanding debt.

### OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The basic financial statements include the following:

- Management's Discussion and Analysis (MD&A), this section
- Basic financial Statements which include:
  - Two kinds of financial statements that present different views of the Division - the Government-Wide Financial Statements and the Fund Financial Statements.
  - The Notes to the Financial Statements that explain some of the information in the financial statements and provide more detail.

### Government-wide Statements

Government-wide financial statements provide both long-term and short-term information about the Division's financial condition. Changes in the Division's financial position may be measured over time by increases and decreases in the Statement of Net Assets. Information on how the Division's net assets changed during the fiscal year are presented in the Statement of Activities.

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**Fund Financial Statements**

The fund financial statements focus on the individual parts of the Division, reporting the Division's operations in more detail than the government-wide financial statements. Fund financial statements can include the statements for governmental, proprietary, and fiduciary funds. The Division has only governmental funds.

**Notes to the Financial Statements**

Notes to the financial statements provide additional information that is essential to the full understanding of the data provided in the government-wide and fund financial statements.

Refer to Note 1 to the financial statements for more detailed information on the elements of the financial statements. The following Table summarizes the major features of the basic financial statements:

**Major Features of the Basic Financial Statements**

	Government-wide Financial Statements	Fund Financial Statements
<b>Scope</b>	Entire Division	Activities of the Division that are not proprietary or fiduciary
<b>Required financial statements</b>	<ul style="list-style-type: none"> <li>• Statement of net assets</li> <li>• Statement of activities</li> </ul>	<ul style="list-style-type: none"> <li>• Balance sheet</li> <li>• Statement of revenues, expenditures, and changes in fund balances</li> </ul>
<b>Accounting basis and measurement focus</b>	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus
<b>Type of asset/liability information</b>	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets included
<b>Type of inflow/outflow information</b>	All revenues and expenses during the year, regardless of when cash is received or paid	<ul style="list-style-type: none"> <li>• Revenues for which cash is received during or soon after the end of the year</li> <li>• Expenditures when goods or services have been received and payment is due during the year or soon thereafter.</li> </ul>

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**CONDENSED FINANCIAL INFORMATION**

**Condensed Statement of Net Assets**

The following condensed financial information was derived from the government-wide statement of net assets and summarizes the Division's net assets as of June 30, 2003 and 2002 (amounts in thousands).

**Net Assets as of June 30**

	<u>2003</u>	<u>2002</u>	<u>% Change</u>
Total current assets	\$ 282,141	\$ 358,432	(21.28%)
Capital assets, net of accumulated depreciation	6,245,789	5,979,536	4.45%
Other non-current assets	<u>3,199</u>	<u>3,574</u>	(10.49%)
Total assets	<u>6,531,129</u>	<u>6,341,542</u>	2.99%
Current liabilities	125,696	155,607	(19.22%)
Long term liabilities	<u>565,250</u>	<u>581,272</u>	(2.76%)
Total liabilities	<u>690,946</u>	<u>736,879</u>	(6.23%)
Invested in capital assets, net of related debt	5,756,415	5,519,388	4.29%
Unrestricted	<u>83,768</u>	<u>85,275</u>	(1.77%)
Total net assets	<u>\$ 5,840,183</u>	<u>\$ 5,604,663</u>	4.20%

The largest component(98.57%) of the Division's net assets reflects its investment in capital assets (e.g. land, buildings, equipment, infrastructure and others) less any related debt outstanding (excluding debt proceeds that have yet to be expended for infrastructure construction) that was needed to acquire or construct the assets. The Division uses these capital assets to provide services to the citizens and businesses in the State; consequently, these net assets are not available for future spending. The remaining portion, unrestricted net assets, may be used at the Division's discretion.



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MANAGEMENT'S DISCUSSION AND ANALYSIS

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**Condensed Statement of Activities**

The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the Division's net assets changed during the fiscal year (amounts in thousands):

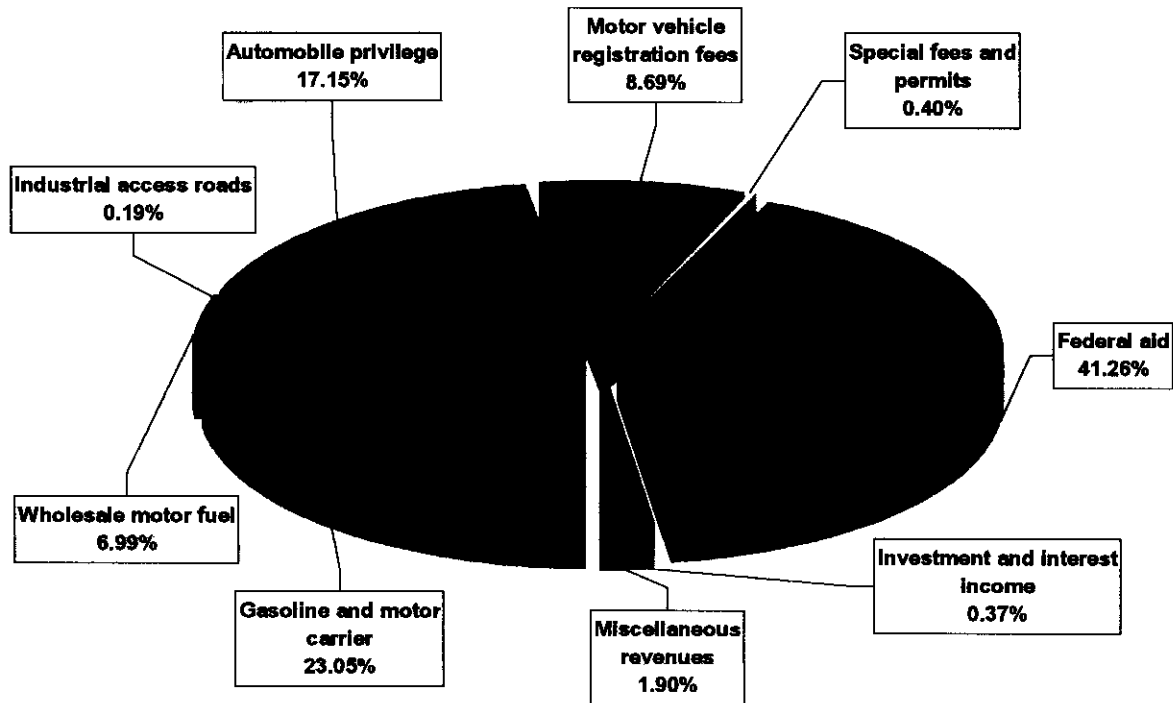
	<u>2003</u>	<u>2002</u>	<u>% Change</u>
<b>Revenues</b>			
Taxes	\$ 466,273	\$ 481,436	(3.15%)
Licenses, fees and permits	85,880	87,380	(1.72%)
Investment and interest income	3,655	8,148	(55.14%)
Miscellaneous revenues	18,793	15,062	24.77%
Total general revenues	<u>574,601</u>	<u>592,026</u>	(2.94%)
Federal aid	409,555	437,070	(6.30%)
Charges for service	3,965	4,173	(4.98%)
Total program revenues	<u>413,520</u>	<u>441,243</u>	(6.28%)
Total revenues	<u>988,121</u>	<u>1,033,269</u>	(4.37%)
<b>Expenses</b>			
Road maintenance	315,921	309,684	2.01%
Other road operations	329,531	380,281	(13.35%)
General and administration	77,619	85,822	(9.56%)
Interest on long-term debt	27,434	28,168	(2.61%)
Unallocated depreciation	2,096	2,267	(7.54%)
Total expenses	<u>752,601</u>	<u>806,222</u>	(6.65%)
Change in net assets	235,520	227,047	3.73%
Net assets, beginning	<u>5,604,663</u>	<u>5,377,616</u>	4.22%
Net assets, ending	<u>\$ 5,840,183</u>	<u>\$ 5,604,663</u>	4.20%

Over time, increases and decreases in net assets measure whether the Division's financial position is improving or deteriorating. During the fiscal year, the net assets of the governmental activities increased by \$236 million or 4.20% percent.

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MANAGEMENT'S DISCUSSION AND ANALYSIS

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The following chart depicts the revenues of the Division for the fiscal year.



Total revenues decreased by approximately \$45 million. Total tax revenues decreased by approximately \$15 million with the majority of the decrease (\$11 million or 66.26%) due to a decline in automobile privilege tax. Federal aid revenue decreased by approximately \$26 million (5.89%). The following summarizes revenues for the years ended June 30, 2003 and June 30, 2002 (amounts in thousands):

	2003	2002	Increase (decrease)	% Increase (decrease)
Gasoline and motor carrier road tax	\$ 227,793	\$ 229,650	\$ (1,857)	(.81%)
Wholesale motor fuel	69,049	71,314	(2,265)	(3.18%)
Industrial access roads	1,891	3,914	(2,023)	(51.69%)
Automobile privilege	169,431	180,472	(11,041)	(6.12%)
Motor vehicle registration fees	85,880	87,380	(1,500)	(1.72%)
Special fees and permits	3,965	4,173	(208)	(4.98%)
Federal aid	407,664	433,156	(25,492)	(5.89%)
Investment and interest income	3,655	8,148	(4,493)	(55.14%)
Miscellaneous revenues	18,793	15,062	3,731	24.77%
	<u>\$ 988,121</u>	<u>\$ 1,033,269</u>	<u>\$ (45,148)</u>	<u>(4.37%)</u>

The Division's primary sources of revenue for funding of ongoing administration of the Division, general maintenance and construction of the State Road System and for providing resources to match available Federal funds is derived from fuel taxes, automobile privilege tax, motor vehicle registration and license fees, net of costs incurred by the Division of Motor Vehicles in collecting funds for deposit into the State Road Fund.

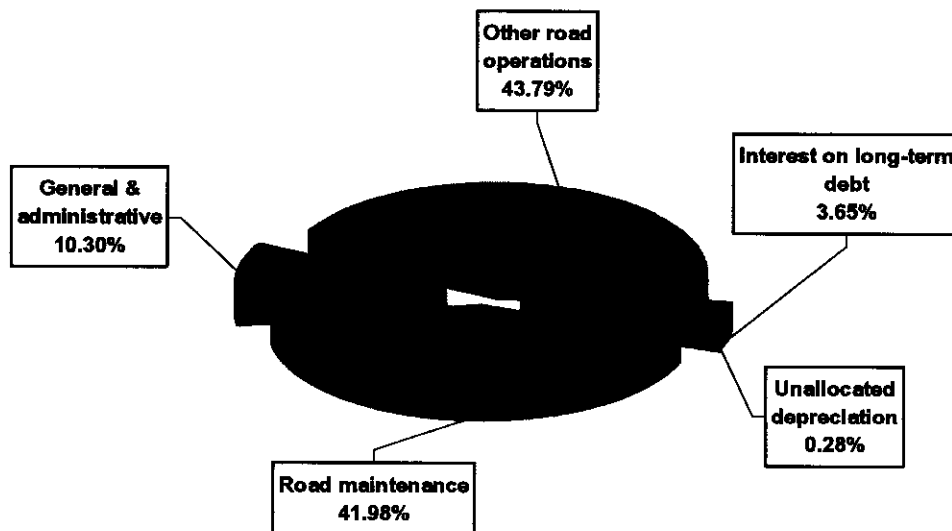
WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
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MANAGEMENT'S DISCUSSION AND ANALYSIS

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Tax collections, especially of automobile privilege tax, exceeded official estimates by a significant amount during the past several years, allowing the Division to undertake additional projects and expand customer services. Unfortunately, both the state and national economies have slowed dramatically. The result was significant reductions in automobile privilege tax collections for the 2003 year. Revenues are projected to remain relatively flat through fiscal year 2006 at the same time it is anticipated that nondiscretionary costs will continue to rise. As a consequence, many programs that operate from the Division will experience little, if any, increase in the foreseeable future and some programs may be funded at lower levels.

The Division also relies on Federal funds as a source of revenue. The Federal Aid is obtained in the form of reimbursable grants. Federal funds received during 2003 were authorized under the "Transportation Equity Act for the 21<sup>st</sup> Century" (TEA21). The recognition of revenue under these grants occurs when expenditures occur on specific projects that have qualified for federal participation. While Federal transportation legislation and special spending authorizations result in funds available for obligation by the Federal Government in specific years, and the Division expects to continue to fully obligate available funds, thus ensuring that all available Federal dollars are received by the Division, the timing of revenue recognition for financial reporting is dependent on the timing of completion of specific construction projects. TEA 21 expired in 2003. The United States Congress is currently working on reauthorization of a new Highway Transit Bill (TEA 3). The results of the reauthorization are yet to be determined.

The following chart depicts expenses of the Division for the fiscal year.



Total expenses decreased by approximately \$54 million (6.65%). The following summarizes expenditures for the years ended June 30, 2003 and June 30, 2002 (amounts in thousands):

	2003	2002	Increase (decrease)	% Increase (decrease)
Road maintenance	\$ 315,921	\$ 309,684	\$ 6,237	2.01%
Other road operations	329,531	380,281	(50,750)	(13.35%)
General and administration	77,619	85,822	(8,203)	(9.56%)
Interest on long-term debt	27,434	28,168	(734)	(2.61%)
Unallocated depreciation	2,096	2,267	(171)	(7.54%)
	<u>\$ 752,601</u>	<u>\$ 806,222</u>	<u>\$ (53,621)</u>	<u>(6.65%)</u>

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The maintenance expenses of the Division are composed primarily of routine maintenance, small bridge repair, and contract paving.

The type of routine maintenance expenses incurred is dependent, to a degree, on the level of snow and ice removal that is required in a given year. Operating divisions are allocated amounts for routine maintenance in the Division's annual plan. The State had a relatively severe winter during the year ended June 30, 2003 and incurred approximately \$27 million in costs in excess of those incurred in the prior year. This increase was offset to a large degree by cost containment measures implemented during the year.

Other road operations expenditures reported in the Government-Wide Financial Statements include the total expended for all other road operations and small construction activities that fail to meet the criteria established for capitalization as infrastructure assets. A discussion of the change in actual funds expended is included in the financial analysis of the Division's Fund Financial Statements below.

#### **FINANCIAL ANALYSIS OF THE DIVISION'S MAJOR FUNDS**

As the Division completed the year, the Division reported fund balances of \$203 million. Of this total amount, \$144 million, 70.96%, constitutes unreserved fund balance, which is available for appropriation for the general purposes of the funds. The remainder of fund balance is reserved and is not available for new spending because it has already been dedicated for various commitments, such as capital outlay projects.

##### **State Road Fund**

The State Road Fund is the Division's General Fund. At the end of the 2003 fiscal year, unreserved fund balance of the General fund was \$144 million and reserved fund balance was \$27 million. The total General fund balance increased \$8 million during the year primarily due to cost containment measures instituted which offset the lower than anticipated tax revenues and the impact of the severe winter as discussed above in the financial analysis of the Division as a whole.

##### **Capital Projects Fund**

The Capital Projects Fund is used to account for financial resources to be used for road construction or reconstruction financed by the proceeds from the sale of Safe Road Bonds and matching federal highway funds on such projects. At June 30, 2003, the fund balance of the fund represented unexpended bond funds associated with the 2002 bond issue. The projects to be constructed from the proceeds of these bonds have been programmed, and where applicable, the federal funds for the projects have been obligated.

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**State Road (General) Fund and Budgetary Highlights**

The Division is dependent on revenues generated from the purchase and use of motor fuel, motor vehicle fees, privilege tax on consumer purchases of motor vehicles, and federal funding generated from motor fuel purchases. Revenues are affected by state and national economic conditions, world events affecting availability and pricing of motor fuel and fuel consumption rates for motor vehicles. Although average fuel consumption rates for motor vehicles have remained fairly constant over the past several years, any future changes in consumption rates would have a significant impact on revenue collections unless there is a corresponding change to the tax rates or structure. For the previous six years, tax and fee revenue collections increased over the previous year. However, tax and fee revenue collections declined by approximately \$17 million during the current year. The following table summarizes tax and fee collection over the past four years (amounts in thousands):

	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2003 vs. 2002</u>	
				<u>Change</u>	<u>%Change</u>
Gasoline and motor carrier	\$ 225,946	\$ 229,650	\$ 227,793	\$ (1,857)	(.81%)
Sales tax on fuel - wholesale	71,521	71,314	69,049	(2,265)	(3.18%)
Motor vehicle registration	78,745	87,380	85,880	(1,500)	(1.72%)
Privilege tax	<u>155,623</u>	<u>180,472</u>	<u>169,431</u>	<u>(11,041)</u>	<u>(6.12%)</u>
	<u>\$ 531,835</u>	<u>\$ 568,816</u>	<u>\$ 552,153</u>	<u>\$ (16,663)</u>	<u>(2.93%)</u>

Automobile privilege tax collections were positively impacted in 2002 by low interest rates and significant incentives offered by automobile manufacturers. It is possible that the automobile privilege taxes could decline significantly when these factors no longer exist and that declines in automobile privilege tax revenues could continue. Declining motor fuel collections reflect the current economic weakness and the impact of the war in Iraq that have lead to falling fuel consumption.

The Division's budget included \$397 million in federal aid revenues to be used primarily for design, right-of-way and construction of Corridor D, Corridor H, WV 9 and other major corridors including King Coal Highway, Coalfields Expressway, WV 2, WV 10, and WV 35. As previously discussed the recognition of revenue under these grants occurs when expenditures occur on specific projects that have qualified for federal participation. Since the timing of such expenditures are dependent on variables such as the weather, the existence of differing site conditions that require plan modification, or delays caused by environmental issues or the results of public meetings, expenditures often do not occur as planned. The budgeted amounts for federal aid revenue and expenditures are based on projects that have been approved and estimates of the timing of each phase of the project. Federal Aid revenue in each of the last three years are summarized below (amounts in thousands):

	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>Change</u>	<u>%Change</u>
Federal reimbursement - budgeted funds	\$ 374,138	\$ 371,548	\$ 380,079	\$ 8,531	2.30%
Federal reimbursement - bond funds	35,802	47,139	23,129	(24,010)	(50.93%)
Federal reimbursement - emergency funds	<u>2,464</u>	<u>14,469</u>	<u>4,456</u>	<u>(10,013)</u>	<u>(69.20%)</u>
Total federal aid	<u>\$ 412,404</u>	<u>\$ 433,156</u>	<u>\$ 407,664</u>	<u>\$ (25,492)</u>	<u>(5.89%)</u>

The State of West Virginia had a severe winter during 2003. As a result, expenditures for snow and ice removal were in excess of the amounts initially budgeted. With total cost of approximately \$45 million, the winter of 2002-2003 was almost exactly double West Virginia's five-year average of \$23 million for snow removal and ice control and half again as much as the previous record expenditure of \$31 million.

As a result of the above items, the original budget was amended. The most significant changes were:

- Decrease anticipated federal aid expenditures and the related revenues by approximately \$67 million
- Increase in maintenance expenditures by approximately \$42 million

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There were no over expenditures by the Division in appropriated funds. In addition, there were no over expenditures in specific budget line items.

Although it is anticipated that revenues will increase slightly in the next fiscal year, the Division's revenue increases are not projected to keep pace with increases in costs related to retirement, health insurance, increased debt service and other increases that are non-discretionary in nature. As a result the Division will be required to reduce expenditures on programs that are discretionary and expenditures in these areas will be managed to ensure that the Division maintains a positive fund balance. The fiscal 2004 budget reflects a budgeted increase in fund balance of approximately \$53 million. A portion of this increase is based on projected increase in tax collections as a result of implementation of new legislation that moves the point of fuel tax taxation from the distribution to the rack. Management is taking all necessary steps to ensure that the fund balance of the Division is maintained at levels that are adequate to ensure the soundness of the Division and is confident that adequate discretionary items exist to permit them to continue to operate in a fiscally sound manner. However, the level of funding available and the increases in non-discretionary spending may impact the Division's ability to achieve all operational objectives.

## **CAPITAL ASSETS AND DEBT ADMINISTRATION**

### **Capital Assets**

As of June 30, 2003, the Division had invested \$6.2 billion, net of accumulated depreciation, in a range of capital assets (see note 6 for additional details). Depreciation charges for the fiscal year totaled \$244 million.

The \$266 million increase in capital assets, net of depreciation, reflects the nature of the State's road system. While the Division continues to expand the state road system, these expansions are focused primarily on upgrading existing roadways and completion of Appalachian Highway Corridors. While these are significant construction projects, the additions are offset by \$244 million in depreciation on the infrastructure. The Division expended \$515 million dollars during the year ended June 30, 2003 for additions to infrastructure. Of this amount, \$491 million was related to the acquisition of right of way and construction of roads and bridges. Construction costs for completed projects in the amount of \$352 million were reclassified from construction in process to roads and bridges. Major construction expenditures during the year included continued construction related to Corridor H in Randolph and Hardy Counties, Corridor D in Wood County, upgrade of WV 10 in Logan County, upgrade of WV 2 in Brooke County, widening of I-64, and continued environmental studies on various projects in process.

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MANAGEMENT'S DISCUSSION AND ANALYSIS

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### Long-term Debt

The Division has been authorized to issue bonds by constitutional amendments and all bonds are general obligation bonds of the State of West Virginia. All bonds authorized under prior constitutional amendments have been issued. At June 30, 2003, the Division had \$518 million in outstanding bonds. The amount outstanding decreased by \$22 million (4.08%) due to principal payments of \$22 million.

The following is a summary of the amounts outstanding, including insured status and bond ratings:

Issue	Status of insurance	Bond Rating		Amount (in thousands)	
Better Highways 73 - All Bonds maturing on or before June 1, 2006	Not insured	Fitch:	AA-	\$	10,815
		Moody's:	Aa3		
		S&P:	AA-		
Safe Roads 98A - All Bonds maturing on or before June 1, 2023	Insured by FGIC	Fitch:	AAA		199,750
		Moody's:	Aaa		
		S&P:	AAA		
Safe Roads 99A - All Bonds maturing on or before June 1, 2007	Not Insured	Fitch:	AA-		103,270
		Moody's:	Aa3		
		S&P:	AA-		
Safe Roads 00A - All Bonds maturing on or before June 1, 2020	Insured by FGIC	Fitch:	AAA		32,290
		Moody's:	Aaa		
		S&P:	AAA		
Safe Roads 00A - Term Bond maturing on June 1, 2025	Insured by MBIA	Fitch:	AAA		77,710
		Moody's:	Aaa		
		S&P:	AAA		
Safe Roads 01A - Bonds maturing between June 1, 2005 to 2013	Insured by FSA	Fitch:	AAA		93,465
		Moody's:	Aaa		
		S&P:	AAA		
Safe Roads 01A - Bonds maturing in 2004	Not insured	Fitch:	AA-		200
		Moody's:	Aa3		
		S&P:	AA-		
				\$	517,500

More detailed information regarding capital asset and long-term debt activity is included in the notes to the financial statements.

BASIC FINANCIAL STATEMENTS
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WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
STATEMENT OF NET ASSETS  
JUNE 30, 2003  
(amounts expressed in thousands)

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ASSETS	Governmental Activities
Current assets	
Cash and cash equivalents	\$ 129,076
Accounts receivable	55,707
Taxes receivable	64,180
Due from other State of West Virginia agencies	3,691
Inventories	27,461
Other assets	2,026
Total current assets	<u>282,141</u>
Non-current assets	
Capital assets, net of accumulated depreciation	
Land - non-infrastructure	14,650
Land improvements	3,836
Buildings	39,848
Buildings - work in progress	8,105
Furniture and fixtures	446
Rolling stock	48,488
Scientific equipment	613
Shop equipment	224
Roads	3,787,146
Bridges	974,763
Land - infrastructure	647,247
Work in progress	720,423
Total capital assets	<u>6,245,789</u>
Other non-current assets	<u>3,199</u>
Total assets	<u>6,531,129</u>
LIABILITIES	
Current liabilities	
Accounts payable	43,946
Retainages payable	12,934
Accrued payroll and related liabilities	18,398
Due to other State of West Virginia agencies	4,044
Accrued interest payable	2,241
Current maturities of long term obligations	44,133
Total current liabilities	<u>125,696</u>
Non-current liabilities	
Claims and judgements	6,400
Compensated absences	61,639
General obligation bonds	497,211
Total non-current liabilities	<u>565,250</u>
Total liabilities	<u>690,946</u>
NET ASSETS	
Invested in capital assets, net of related debt	5,756,415
Unrestricted	<u>83,768</u>
Total net assets	<u>\$ 5,840,183</u>

The Accompanying Notes Are An Integral  
Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
STATEMENT OF ACTIVITIES  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

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Functions/Programs	Expenses	Program Revenues		Net Revenue (Expenses) and Changes in Net Assets
		Charges for Services	Capital Grants and Contributions	
Government activities				
Road maintenance				
Expressway, trunkline & feeder & SLS	\$ 237,026	\$ -	\$ -	\$ (237,026)
Contract paving & secondary roads	43,417	-	-	(43,417)
Small bridge repair & replacement	21,580	-	-	(21,580)
Litter control program	1,492	-	-	(1,492)
Depreciation	12,406	-	-	(12,406)
Other road operations				
Interstate highways	3,152	-	44,372	41,220
Appalachian highways	-	-	168,789	168,789
Other federal aid programs	83,240	-	194,503	111,263
Non federal aid improvements	12,688	-	-	(12,688)
Industrial access roads	523	-	1,891	1,368
Depreciation	229,928	-	-	(229,928)
General and administration				
Support and administrative operations	40,964	3,965	-	(36,999)
Claims	2,461	-	-	(2,461)
Costs associated with DMV	34,194	-	-	(34,194)
Interest on long-term debt	27,434	-	-	(27,434)
Unallocated depreciation	2,096	-	-	(2,096)
	<u>752,601</u>	<u>3,965</u>	<u>409,555</u>	<u>(339,081)</u>
General revenues				
Taxes:				
				227,793
Gasoline and motor carrier				69,049
Wholesale motor fuel				169,431
Automobile privilege				85,880
Motor vehicle registration fees				3,655
Investment and interest income				18,793
Miscellaneous revenues				
Total general revenues				<u>574,601</u>
Change in net assets				235,520
Net assets, beginning (as restated)				<u>5,604,663</u>
Net assets, ending				<u>\$ 5,840,183</u>

The Accompanying Notes Are An Integral  
Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
BALANCE SHEET - GOVERNMENTAL FUNDS  
JUNE 30, 2003  
(amounts expressed in thousands)

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	State Road (General)	Capital Projects	Total Governmental Funds
<b>ASSETS</b>			
Assets			
Cash and cash equivalents	\$ 94,514	\$ 34,562	\$ 129,076
Receivables	54,754	953	55,707
Taxes receivable	64,180	-	64,180
Due from other State of West Virginia agencies	3,691	-	3,691
Due from other funds	-	178	178
Inventories	27,461	-	27,461
Other assets	2,026	-	2,026
Total assets	<u>\$ 246,626</u>	<u>\$ 35,693</u>	<u>\$ 282,319</u>
<b>LIABILITIES AND FUND BALANCES</b>			
Liabilities			
Accounts payable	\$ 41,319	\$ 2,627	\$ 43,946
Retainages payable	11,298	1,636	12,934
Accrued payroll and related liabilities	18,398	-	18,398
Due to other State of West Virginia agencies	4,044	-	4,044
Due to other funds	178	-	178
Total liabilities	<u>75,237</u>	<u>4,263</u>	<u>79,500</u>
Fund balances			
Reserved for capital projects	-	31,430	31,430
Reserved for inventories	27,461	-	27,461
Unreserved, undesignated	143,928	-	143,928
Total fund balances	<u>171,389</u>	<u>31,430</u>	<u>202,819</u>
Total liabilities and fund balances	<u>\$ 246,626</u>	<u>\$ 35,693</u>	<u>\$ 282,319</u>

The Accompanying Notes Are An Integral  
Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS  
TO THE STATEMENT OF NET ASSETS  
JUNE 30, 2003  
(amounts expressed in thousands)

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Total fund balances - governmental funds	\$	202,819
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Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. These assets consist of:

Land - non infrastructure	\$	14,650	
Land improvements- non infrastructure		3,836	
Buildings		39,848	
Buildings - work in progress		8,105	
Furniture and Fixtures		446	
Rolling Stock and Shop Equipment		48,488	
Scientific Equipment		613	
Shop Equipment		224	
Roads		3,787,146	
Bridges		974,763	
Infrastructure Land		647,247	
Work in progress		<u>720,423</u>	6,245,789

Bonds issued by the Division have associated costs that are paid from current available financial resources in the funds. However, these costs are deferred on the statement of net assets

3,199

Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:

Accrued interest payable	(2,241)	
Claims and judgments	(6,961)	
Compensated absences	(81,466)	
General obligation bonds	<u>(520,956)</u>	(611,624)

Net assets of governmental activities	\$	<u><u>5,840,183</u></u>
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WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
STATEMENT OF REVENUES, EXPENDITURES, AND  
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

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	State Road (General)	Capital Projects	Total Governmental Funds
Revenues			
Taxes			
Gasoline and motor carrier	\$ 227,793	\$ -	\$ 227,793
Wholesale motor fuel	69,049	-	69,049
Automobile privilege	169,431	-	169,431
Industrial access	1,891	-	1,891
License, fees and permits			
Motor vehicle registrations and licenses	85,880	-	85,880
Special fees and permits	3,965	-	3,965
Federal aid			
Interstate highways	44,226	146	44,372
Appalachian highways	168,789	-	168,789
Other federal aid programs	190,193	4,310	194,503
Investment and interest income, net of arbitrage rebate	1,101	2,554	3,655
Miscellaneous revenues	18,846	-	18,846
	<u>981,164</u>	<u>7,010</u>	<u>988,174</u>
Expenditures			
Current			
Road maintenance			
Expressway, trunkline and feeder, state and local services	238,591	-	238,591
Contract paving and secondary roads	43,417	-	43,417
Small bridge repair and replacement	28,749	-	28,749
Litter control program	1,492	-	1,492
Support and administrative operations	57,655	-	57,655
Division of Motor Vehicles operations	34,194	-	34,194
Claims	595	-	595
Capital outlay and other road operations			
Road construction and other road operations			
Interstate highways	54,404	329	54,733
Appalachian highways	194,507	-	194,507
Other federal aid programs	256,844	5,637	262,481
Nonfederal aid construction and road operations	12,361	53,297	65,658
Industrial access road	523	-	523
Debt service	50,019	-	50,019
	<u>973,351</u>	<u>59,263</u>	<u>1,032,614</u>
Excess (deficiency) of revenues over expenditures	7,813	(52,253)	(44,440)
Fund balances, beginning of year	<u>163,576</u>	<u>83,683</u>	<u>247,259</u>
Fund balances, end of year	<u>\$ 171,389</u>	<u>\$ 31,430</u>	<u>\$ 202,819</u>

The Accompanying Notes Are An Integral  
Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS

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RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES  
IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

Net change in fund balances - total governmental funds \$ (44,440)

Amounts reported for governmental activities in the statement of activities  
are different because:

Governmental funds report capital outlays as expenditures. However, in the  
statement of activities, the cost of those assets is allocated over their  
estimated useful lives as depreciation expense. This is the amount by which  
capital outlays of \$511,467 exceeded depreciation of (\$244,430) in the  
current period.

267,037

Governmental funds report the proceeds from the sale of capital assets,  
primarily equipment, as revenue. In the statement of activities revenues is  
only recognized to the extent that amounts received are in excess of the net  
book value of the assets sold. The net book value of assets disposed of  
during the year was (\$785).

(785)

Repayment of bond principal is an expenditure to governmental funds, but  
the repayment reduces long-term liabilities in the statement of net assets.

22,040

Some expenses reported in the statement of activities do not require the use  
of current financial resources and therefore are not reported as expenditures  
in the governmental funds. This is the amount by which the increase in  
compensated absences of (\$7,012), accrued claims of (\$1,865) and  
amortization of bond issuance costs of (\$375) exceeded accretion of bond  
premiums of \$835 and a decrease in interest payable of \$85.

(8,332)

Change in net assets of governmental activities

\$ 235,520

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION, DIVISION OF HIGHWAYS  
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL  
(BUDGETARY BASIS) - STATE ROAD FUND  
YEAR ENDED JUNE 30, 2003

(amounts expressed in thousands)

	Original Budget	Budget Amendments	Final Budget	Actual Amounts	Variance with Final Budget - Positive (Negative)
Revenues					
Taxes					
Gasoline and motor carrier	\$ 226,960	\$ -	\$ 226,960	\$ 220,463	\$ (6,497)
Wholesale motor fuel	72,100	-	72,100	67,576	(4,524)
Automobile privilege	160,868	12,000	172,868	170,478	(2,390)
Motor vehicle registrations and licenses	79,490	-	79,490	85,836	6,346
Federal aid	511,204	(66,910)	444,294	396,631	(47,663)
Miscellaneous revenues	9,000	(3,350)	5,650	8,049	2,399
	<u>1,059,622</u>	<u>(58,260)</u>	<u>1,001,362</u>	<u>949,033</u>	<u>(52,329)</u>
Expenditures					
Road construction and other road operations					
Interstate highways	70,000	(10,000)	60,000	55,198	4,802
Appalachian highways	225,000	(17,000)	208,000	199,670	8,330
Other federal aid programs	325,700	(41,000)	284,700	234,569	50,131
Nonfederal aid construction	20,000	2,000	22,000	14,463	7,537
Road maintenance					
Maintenance	243,700	41,500	285,200	247,250	37,950
Contract paving and secondary roads	45,000	3,500	48,500	45,390	3,110
Small bridge repair and replacement	34,000	(3,000)	31,000	29,066	1,934
Litter control program	1,490	-	1,490	1,490	-
Support and administrative operations					
General operations	43,768	-	43,768	37,019	6,749
Equipment revolving	15,000	-	15,000	14,119	881
Inventory revolving	2,000	-	2,000	(1,959)	3,959
Debt service	50,000	-	50,000	49,798	202
Division of Motor Vehicles operations	38,219	-	38,219	34,194	4,025
Waste tire	3,625	-	3,625	2,004	1,621
Claims	595	-	595	595	-
	<u>1,118,097</u>	<u>(24,000)</u>	<u>1,094,097</u>	<u>962,866</u>	<u>131,231</u>
Excess (deficiency) of revenues over expenditures	(58,475)	(34,260)	(92,735)	(13,833)	78,902
Fund balance, beginning of year	<u>105,992</u>	<u>-</u>	<u>105,992</u>	<u>105,992</u>	<u>-</u>
Fund balance, end of year	<u>\$ 47,517</u>	<u>\$ (34,260)</u>	<u>\$ 13,257</u>	<u>\$ 92,159</u>	<u>\$ 78,902</u>

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The Accompanying Notes Are An Integral  
Part Of These Financial Statements

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
NOTES TO THE FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**BASIS OF PRESENTATION** - The accompanying financial statements of the West Virginia Department of Transportation, Division of Highways (the Division) have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

**REPORTING ENTITY** - The Division is an operating unit of the West Virginia Department of Transportation and represents separate funds of the State of West Virginia (the State) that are not included in the State's general fund. The Division is a legally separate entity defined by the State constitution, and has statutory responsibility for the construction, reconstruction, maintenance, and improvement of all State roads. The Division is governed by a commissioner who is appointed by the Governor, but does not have a governing board separate from the State Legislature. The Division is considered a component unit of the State and its financial statements are blended with the financial statements of the primary government in the state's comprehensive annual financial report.

The financial statements of the Division are intended to present the financial position, and the results of operations of only that portion of the financial reporting entity of the West Virginia Department of Transportation and the State of West Virginia, that is attributable to the transactions of the Division. They do not purport to, and do not, present fairly the financial position of the West Virginia Department of Transportation or the State of West Virginia as of June 30, 2003 and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management has considered all potential component units to be included in the Division's reporting entity by applying the criteria set forth in accounting principles generally accepted in the United States of America. These criteria include consideration of organizations for which the Division is financially accountable, or organizations for which the nature and significance of their relationship with the Division are such that exclusion would cause the Division's financial statements to be misleading or incomplete. Since no organizations meet these criteria, the Division has no component units.

The Division of Motor Vehicles is an operating division of the West Virginia Department of Transportation, which collects certain revenues for expenditure by the Division. The expenditures related to the collection of these revenues are recorded in the State Road Fund of the Division.

**GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS** - The government-wide financial statements (the statement of net assets and the statement of activities) report information of all of the non-fiduciary activities of the primary government and its component units, if any. For the most part, the effect of interfund activity has been removed from these government-wide statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component units for which the primary government is financially accountable. The Division has no component units, fiduciary activities or business type activities; therefore, the government-wide financial statements of the Division are composed of all of the governmental activities of the Division.

The statement of activities demonstrates the degree to which the direct expenses of a given function, segment or component unit are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function, segment, or component unit. Program revenues include charges to customers who purchase, use or directly benefit from goods or services provided by a given function, segment, or component unit. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function, segment, or component unit. Taxes and other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues. The Division does not allocate general government (indirect) expenses to other functions.



WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
NOTES TO THE FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets.

When both restricted and unrestricted resources are available for use, generally it is the Division's policy to use restricted resources first, then unrestricted resources, as they are needed. Separate financial statements are provided for governmental funds, proprietary funds, fiduciary funds and similar component units, and major component units, if applicable. However, the fiduciary funds are not included in the government-wide statements. Major individual governmental funds and major individual enterprise funds, if applicable, are reported as separate columns in the fund financial statements.

MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION -

**GOVERNMENT-WIDE FINANCIAL STATEMENTS** - The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

**GOVERNMENTAL FUND FINANCIAL STATEMENTS** - The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Division considers revenues to be available if they are collected within 60 days of the end of the current fiscal year. Principal revenues subject to accrual include gasoline and wholesale fuel taxes, automobile privilege taxes, federal reimbursements and other reimbursements for use of materials and services.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting for the governmental fund financial statements include:

- Employees' vested annual leave is recorded as expenditures when utilized. The amount of accumulated annual leave unpaid at June 30, 2003, has been reported only in the government-wide financial statements.
- Division employees earn sick leave benefits, which accumulate, but do not vest. When separated from employment with the Division, an employee's sick leave benefits are considered ended and no reimbursement is provided. However, an employee may convert, at the time of retirement, any unused accumulated sick leave to pay a portion of the employee's post employment health care insurance premium or to increase service credits for retirement purposes. The liability for accumulated sick leave for employees has been recorded only in the government-wide financial statements.
- The Division pays 100% of the health insurance premium for retirees who elected to participate in the health insurance plans prior to July 1, 1988 and 50% of the premium for retirees who elected to participate prior to July 1, 2001. The liability for accumulated post-retirement health insurance has been reported only in the government-wide financial statements.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
NOTES TO THE FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

- Principal and interest on general long-term debt are recorded as fund liabilities when due or when amounts have been accumulated in the debt service fund for transfer to the fiscal agent or for payment to be made early in the following year.
- Claims and judgments are recorded only when payment is due.

**FUND ACCOUNTING** - The Division uses funds to report its financial position and the results of its operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fund is a separate accounting entity with a self-balancing set of accounts. The following summarizes the major governmental funds that are presented in the accompanying financial statements:

- **State Road (General) Fund** - This fund serves as the Division's general fund and is used to account for all financial resources, except those required to be accounted for in another fund. The State Road Fund is funded primarily by dedicated highway user taxes and fees and matching federal highway funds.
- **Capital Projects Fund** - This fund accounts for financial resources to be used for road construction or reconstruction financed by proceeds from the sale of the Safe Road Bonds and matching federal highway funds.

**INTERFUND ACTIVITY** - As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges from the government's various functions. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned. The Division processes certain routine payments, such as payroll through the State Road Fund and allocates those costs to the Capital Project Fund based on individual projects charged. The interfund balances at June 30, 2003 are a result of these routine payments and transfers.

**BUDGETING AND BUDGETARY CONTROL** - The Division's expenditures are subject to the legislative budget process of the State, with annual budgets adopted utilizing the cash basis of accounting. The cash basis is modified at year-end to allow for payment of invoices up to 31 days after year-end for goods or services received prior to year-end. Appropriated budgeted expenditures, which lapse 31 days after the end of the fiscal year, are incorporated into the Division's overall financial plan, which includes revenue estimates developed by the Division and the State's executive branch. Expenditures are budgeted using natural categories of activity including specific categories of construction, maintenance, and operations, as well as for special items. Any revisions that alter budgeted expenditures for the expenditure categories for each Division as a whole must be approved by the State Legislature.

The Division's State Road Fund has a legislatively approved budget. However, the capital projects fund, debt service fund, and certain monies reported within the State Road Fund for GAAP purposes, are not considered appropriated funds in accordance with the Division's budgetary reporting policy. Accordingly, these funds have not been reported in the Division's Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual (Budgetary Basis) - State Road Fund. A reconciliation of the excess of revenues over expenditures and other financing uses for the year ended June 30, 2003 on the budgetary basis to the GAAP basis for the State Road Fund follows:

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
NOTES TO THE FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Excess of revenues over expenditures - budgetary basis	\$ (13,833)
Basis of accounting differences (budgetary to GAAP)	21,783
Unbudgeted funds	<u>(137)</u>
Excess of revenues over expenditures - GAAP basis.	<u>\$ 7,813</u>

**CASH AND CASH EQUIVALENTS** - Cash and cash equivalents are short-term investments with original maturities of 90 days or less. Cash and cash equivalents principally consist of amounts on deposit in the State Treasurer's Office (STO) that are pooled funds managed by the West Virginia Investment Management Board (IMB). In addition, the Division makes interest-earning deposits in certain investment pools maintained by the IMB that are available to the Division with overnight notice. Interest income from these investments is prorated to the Division at rates specified by the IMB based on the balance of the Division's deposits maintained in relation to the total deposits of all state agencies participating in the pool. Because these deposits are held in the IMB investment pools, no other disclosures related to safekeeping, credit or market risk, or GASB 3 risk are required. However, market risk exists as the value of the investment pools underlying investment assets may decline because of an increase in interest rates or a decline in stock prices. The carrying value of the deposits reflected in the financial statements approximates fair value and approximates the value of the shares in the external investment pool.

The STO has statutory responsibility for the daily cash management activities of the State's agencies, departments, boards, and commissions. The STO determines which funds to transfer to the IMB for investment in accordance with the West Virginia Code, policies set by the IMB, and provisions of bond indentures and trust agreements when applicable. The IMB is governed by a thirteen-member Board of Trustees. The Governor, the State Auditor and the State Treasurer are members of the Board and the other members are appointed by the Governor. The Board was formed in 1997 to serve as the Trustee to hold certain public pension funds and insurance funds, as well as to provide prudent fiscal administration, investment, and management of the Consolidated Pension Fund and the State's operating funds.

The Divisions cash and cash equivalents were comprised of the following at June 30, 2003:

Investments with IMB	\$ 114,939
Cash	13,938
Cash in transit	<u>199</u>
	<u>\$ 129,076</u>

**INVENTORIES** - Inventories are stated at weighted average cost generally using the "consumption Method" whereby expenditures are recognized in the period in which inventory usage, as opposed to purchase, occurs. The portion of fund balance relating to inventories is reported as "Reserve for inventories" in the Government Fund Financial Statements.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
NOTES TO THE FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

**CAPITAL ASSETS** - Capital assets, which include buildings, non-infrastructure land, furniture and fixtures, rolling stock, scientific equipment, shop equipment and infrastructure assets (which are normally immovable and of value only to the Division, such as roads, bridges, and similar items), are reported in the statement of net assets in the government-wide financial statements. Capital assets are defined by the Division as follows:

- Non-infrastructure assets with a useful life of at least three years and:
  - A cost of five thousand dollars or more for machinery, equipment, rolling stock, furniture and fixtures; or
  - An acquisition cost of twenty-five thousand dollars or more for buildings at the date of acquisition; and
- Infrastructure assets with a cost in excess of one million dollars.

Purchased and constructed capital assets are valued at historical cost or estimated historical cost. Donated fixed assets are recorded at their fair market value at the date of donation.

The estimates of historical costs of buildings and other improvements were based on values that were compiled in 1983. Building and non-infrastructure land have been recorded at cost since 1983. Infrastructure constructed from July 1, 1980 to July 1, 2001 has been recorded at estimated historical cost. The estimated historical cost for years 1980-2001 was based on capital outlay expenditures reported by the West Virginia Department of Transportation in the annual reports for those years, less an amount estimated for the historical cost of the acquisition of land for right-of-way. The Division has not capitalized any infrastructure expenditures for assets constructed prior to July 1, 1980, as permitted by GASB 34. The costs of normal maintenance and repairs that do not add to the asset's value or materially extend an asset's useful life are not capitalized. Interest incurred during construction of capital facilities is not capitalized.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements.

Capital assets are depreciated on the straight-line method over the assets' estimated useful lives. There is no depreciation recorded for land and construction in progress. Generally, estimated useful lives are as follows:

- Machinery and equipment: 5 - 20 years
- Buildings: 40 years
- Furniture and fixtures: 3 - 20 years
- Rolling stock: 1 - 20 years
- Scientific equipment: 2 - 25 years
- Infrastructure: roads - 30 years
- Infrastructure: bridges - 50 years

**ACCOUNTS AND TAXES RECEIVABLE** - Accounts receivable in all funds report amounts that have arisen in the ordinary course of business and are stated net of allowances for uncollectible amounts. Governmental fund type receivables consist primarily of amounts due from the Federal government. Interest and investment revenue receivable in all funds consist of revenues due on each investment. Taxes receivable in governmental funds represent taxes subject to accrual, primarily gasoline and wholesale fuel taxes and automobile privilege taxes, which are collected within forty-five days after year end. The uncollectible amounts are based on collection experience and a review of the status of existing receivables.

WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
NOTES TO THE FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2003  
(amounts expressed in thousands)

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NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

**OTHER ASSETS** - Other assets represent payments that reflect costs applicable to future accounting periods and are recorded as other assets in both government-wide and fund financial statements. They are composed primarily of amounts on deposit with West Virginia Workers' Compensation Fund.

**CLAIMS** - Claims awarded against the Division in the West Virginia State Court of Claims must be approved and funded by legislative action. Expenditures in the fund financial statements for such claims are recognized to the extent that claims awarded are approved and funded by the Legislature. A liability for unfunded claims is recorded in the government-wide financial statements when management and the Division's legal section determine that it is probable that a loss has occurred and the loss can be reasonably estimated. Such claims are segregated as either tort or contract actions and estimates of loss are based on an analysis of the individual claims and historical experience.

**COMPENSATED ABSENCES** - Division employees generally earn vacation and sick leave on a monthly basis. Vacation, up to specific limits, is fully vested when earned, and sick leave, while not vesting to the employee prior to retirement, can be carried over to subsequent periods. Any unused vacation and sick leave accumulated at employee retirement vests to the employee and may be provided in the form of post-retirement payment of all or a portion of the employee's health insurance premiums, or as service credits for retirement purposes. Expenditures for compensated absences are recognized as incurred in the governmental fund financial statements. The government-wide financial statements present the cost of accumulated compensated absences as a liability.

**POST EMPLOYMENT BENEFITS** - The Division pays 100% of the health insurance premium for retirees who elected to participate in the health insurance plans prior to July 1, 1988 and 50% of the premium for retirees who elected to participate between that date and July 1, 2001. Employees who were eligible and elected to participate in the Division's health insurance plan at July 1, 1988 and 2001, and who had continuous participation in the Plan since those dates, are eligible for the post retirement benefits. Expenditures for post retirement health insurance premiums are recognized as incurred in the governmental fund financial statements. The government-wide financial statements present the cost of accumulated post-retirement health insurance as a liability.

**RETIREMENT BENEFITS** - The Division's employees are covered by the West Virginia Public Employees Retirement System (PERS), a multi-employer cost-sharing defined benefit pension plan. PERS covers substantially all employees of the Division, with employer contributions prescribed by PERS as a percentage of covered payroll.

**PREMIUMS, DISCOUNTS AND ISSUANCE COSTS** - In the government-wide financial statements long-term debt and other long-term obligations are presented in the columns for governmental activities. Where material, bond and note premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the debt. Bonds and notes payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges in other assets and are amortized over the term of the related debt. In the governmental fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures.

**ARBITRAGE REBATE LIABILITY** - The capital project fund accounts for arbitrage rebate payable, if any, as a liability of the fund. The change in the obligation is recorded as an adjustment to current year interest revenue.

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NOTE 2 - ACCOUNTS RECEIVABLE

Accounts receivable at June 30, 2003 consisted of the following:

Federal aid billed and not paid	\$ 4,024
Federal aid earned but not billed	<u>44,545</u>
Total federal aid receivable	48,569
Other receivables	<u>9,438</u>
Combined total receivables	58,007
Less: allowance for uncollectibles	<u>(2,300)</u>
Net accounts receivable	<u>\$ 55,707</u>

Accounts receivable representing federal aid earned but not billed relate principally to the Federal Highway Administration's (FHWA) participating share of expenditures on highway projects.

NOTE 3 - TAXES RECEIVABLE

Taxes receivable at June 30, 2003 consisted of the following:

Automobile privilege taxes	\$ 26,468
Gasoline and motor fuel taxes	33,686
Registration fees	<u>4,026</u>
	<u>\$ 64,180</u>

NOTE 4 - DUE FROM/TO OTHER STATE OF WEST VIRGINIA AGENCIES

Amounts due from other State of West Virginia agencies at June 30, 2003 consisted of the following:

The Department of Motor Vehicles	\$ 2,959
The Department of Administration	113
West Virginia University	51
Office of Emergency Services	64
The Governor's Office	237
West Virginia State Police	58
West Virginia Building Commission	40
Other agencies	<u>169</u>
	<u>\$ 3,691</u>

Amounts due to other State of West Virginia agencies at June 30, 2003 consisted of the following:

Public Employees Insurance Agency	\$ 1,164
Public Employees Retirement	1,141
Bureau of Employment Programs	1,644
The Department of Administration	30
Division of Corrections	47
Other agencies	<u>18</u>
	<u>\$ 4,044</u>

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NOTE 5 - INVENTORIES

Inventories at June 30, 2003 consisted of the following:

Materials and supplies	\$ 17,797
Equipment repair parts	8,268
Gas and lubrication supplies	<u>1,396</u>
	<u>\$ 27,461</u>

NOTE 6 - CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2003, was as follows:

	Balance July 1, 2002	Increases	Decreases	Balance June 30, 2003
Capital assets not being depreciated:				
Land - non infrastructure	\$ 14,287	\$ 415	\$ 52	\$ 14,650
Land - infrastructure	579,229	68,018	-	647,247
Construction-in-progress - buildings	188	10,452	2,535	8,105
Construction-in-progress - roads	530,596	271,150	277,545	524,201
Construction-in-progress - bridges	<u>122,529</u>	<u>151,757</u>	<u>78,064</u>	<u>196,222</u>
Total capital assets not being depreciated	<u>1,246,829</u>	<u>501,792</u>	<u>358,196</u>	<u>1,390,425</u>
Capital assets being depreciated:				
Buildings	63,231	2,341	785	64,787
Furniture and fixtures	3,555	174	275	3,454
Land improvements - non infrastructure	4,490	551	-	5,041
Rolling stock	171,231	12,959	12,501	171,689
Shop equipment	3,044	10	14	3,040
Scientific equipment	1,962	70	5	2,027
Infrastructure - roads	5,912,428	273,826	-	6,186,254
Infrastructure - bridges	<u>1,108,091</u>	<u>77,892</u>	<u>-</u>	<u>1,185,983</u>
Total capital assets being depreciated	<u>7,268,032</u>	<u>367,823</u>	<u>13,580</u>	<u>7,622,275</u>
Less accumulated depreciation:				
Buildings and improvements	24,046	1,620	727	24,939
Furniture and fixtures	3,045	227	264	3,008
Land improvements - non infrastructure	953	252	-	1,205
Rolling stock	122,922	12,118	11,839	123,201
Shop equipment	2,669	160	13	2,816
Scientific equipment	1,291	128	5	1,414
Infrastructure - roads	2,192,900	206,208	-	2,399,108
Infrastructure - bridges	<u>187,500</u>	<u>23,720</u>	<u>-</u>	<u>211,220</u>
Total accumulated depreciation	<u>2,535,326</u>	<u>244,433</u>	<u>12,848</u>	<u>2,766,911</u>
Total capital assets being depreciated, net	<u>4,732,706</u>	<u>123,390</u>	<u>732</u>	<u>4,855,364</u>
Governmental activities capital assets, net	<u>\$ 5,979,535</u>	<u>\$ 625,182</u>	<u>\$ 358,928</u>	<u>\$ 6,245,789</u>

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NOTE 6 - CAPITAL ASSETS (Continued)

Current year depreciation totaling \$244,433 was allocated as a separate line item in the statement of activities under the major functions of the Division of Maintenance and Improvements. The remaining unallocated depreciation expense is included as a separate line item in the statement of activities. Infrastructure depreciation is primarily related to construction type activities; depreciation of shop and rolling stock assets is primarily related to maintenance type activities; and depreciation of buildings and improvements and furniture and fixtures support all of the various activities of the Division.

A summary of depreciation on each capital asset type follows:

<u>Asset Type</u>	<u>Depreciation</u>
Buildings and improvements	\$ 1,620
Furniture and fixtures	227
Land improvements	<u>252</u>
Total unallocated	<u>2,099</u>
Rolling stock	12,118
Shop equipment	160
Scientific equipment	<u>128</u>
Total road maintenance	<u>12,406</u>
Infrastructure - roads	206,208
Infrastructure - bridges	<u>23,720</u>
Total other road operations	<u>229,928</u>
Total depreciation expense	<u>\$ 244,433</u>

NOTE 7 - RETAINAGES PAYABLE

The Division has entered into an arrangement with the West Virginia Investment Management Board whereby amounts retained from payments to contractors may, at the option of the contractor, be deposited in an interest bearing account in the contractor's name. Retainage payments are made to the contractor when contracts are satisfactorily completed. The funds on deposit in these accounts are not reported as assets of the Division. At June 30, 2003, retainages payable on contracts had been reduced by these amounts on deposit in such accounts by approximately \$8,220.



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NOTE 8 - LONG-TERM OBLIGATIONS

Long-term obligations at June 30, 2003, and changes for the fiscal year then ended are as follows:

	Issue Date	Interest Rates	Maturity Through	Beginning Balance	Additions	Reductions	Ending Balance
General obligation bonds payable from tax revenue:							
Better highway bonds	1973	5.625%-6.10%	02/01/2006	\$ 18,660	\$ -	\$ 7,845	\$ 10,815
Safe road bonds	1998	4.30%-5.25%	06/01/2023	204,080	-	4,330	199,750
Safe road bonds	1999	4.30%-5.75%	06/01/2017	105,020	-	1,750	103,270
Safe road bonds	2000	5.50%-5.75%	06/01/2025	110,000	-	-	110,000
Safe road bonds	2001	3.50%-5.50%	06/01/2013	101,780	-	8,115	93,665
Total general obligation bonds				539,540	-	22,040	517,500
Bond premium				4,290	-	834	3,456
Total general obligation bonds payable net of premium				543,830	-	22,874	520,956
Claims and judgments				5,095	1,866	-	6,961
Compensated absences				74,454	7,012	-	81,466
Total long-term obligations				\$ 623,379	\$ 8,878	\$ 22,874	\$ 609,383

General obligation bond issues are authorized by constitutional amendments and are general obligations of the State of West Virginia. Legislation implementing the amendments require that debt service on the bonds be paid from the State Road Fund and, to the extent that there are insufficient funds therein, from a levy of an annual state tax. All bonds authorized under prior constitutional amendments have been issued and include amounts outstanding above.

Debt service expenditures for debt service funds included interest of \$28,168 for the year ended June 30, 2003. Total debt service costs, exclusive of coupon redemption costs, for each of the next five years and thereafter, on general obligation bonds payable and liquidated through debt service funds, are as follows:

	2004	2005	2006	2007	2008	2009- 2013	2014- 2018	2019- 2023	2024- 2026	Total
General obligation bonds payable from tax revenue:										
Better highway bonds	\$ 6,360	\$ 3,909	\$ 1,567	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 11,836
State road bonds	43,638	46,087	48,431	49,997	49,996	238,610	157,989	117,598	47,037	799,383
Total general obligation bonds	49,998	49,996	49,998	49,997	49,996	238,610	157,989	117,598	47,037	811,219
Less: interest	26,928	25,781	24,628	23,532	22,201	88,105	51,619	27,158	3,767	293,719
Total principal	23,070	24,215	25,370	26,465	27,795	150,505	106,370	90,440	43,270	517,500
Bond premium	675	563	475	400	336	882	125	-	-	3,456
Total principal and bond premium	\$ 23,745	\$ 24,778	\$ 25,845	\$ 26,865	\$ 28,131	\$ 151,387	\$ 106,495	\$ 90,440	\$ 43,270	\$ 520,956

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NOTE 8 - LONG-TERM OBLIGATIONS (Continued)

The portion of long-term and short-term compensated absences, claims payable, and general obligation bonds are as follows:

	Compensated <u>Absences</u>	Claims and <u>Judgments</u>	General Obligation <u>Bonds and</u> <u>Premium</u>	<u>Total</u>
Short-term liability	\$ 19,827	\$ 561	\$ 23,745	\$ 44,133
Long-term liability	<u>61,639</u>	<u>6,400</u>	<u>497,211</u>	<u>565,250</u>
	<u>\$ 81,466</u>	<u>\$ 6,961</u>	<u>\$ 520,956</u>	<u>\$ 609,383</u>

During the year ended June 30, 1972, the State was authorized by constitutional amendment to issue \$500,000 of general obligation bonds to fund highway and road construction projects known as Better Highway Bonds. During the year ended June 30, 1997, the State was authorized by constitutional amendment to issue \$550,000 of general obligation bonds to fund highway and road construction projects known as Safe Road Bonds. These bonds will be repaid from revenues of the State Road Fund. Safe Road Bonds of \$220,000 were issued during July 1998; \$110,000 were issued during July 1999; \$110,000 were issued during July 2000; and an additional \$110,000 were issued during July 2001.

The Division's Safe Road Bonds are subject to the arbitrage rebate provisions of the Internal Revenue Code, which requires 90% of interest earnings in excess of interest expended to be paid to the Internal Revenue Service. The Division has no arbitrage rebate liability as of June 30, 2003.

The following summarizes the estimated claims liability for the current year and that of the preceding two years.

	Year Ended <u>June 30, 2003</u>	Year Ended <u>June 30, 2002</u>	Year Ended <u>June 30, 2001</u>
Estimated claims liability, July 1	\$ 5,095	\$ 11,200	\$ 9,300
Additions for claims incurred during the year	3,246	2,787	1,585
Changes in estimates for claims of prior periods	(785)	(8,877)	415
Payments on claims	<u>(595)</u>	<u>(15)</u>	<u>(100)</u>
Estimated claims liability, June 30	<u>\$ 6,961</u>	<u>\$ 5,095</u>	<u>\$ 11,200</u>

At June 30, 2003, approximately \$19,877 of tort claims and \$5,351 of construction claims, including non-incremental claims, were pending against the Division in the West Virginia State Court of Claims. With respect to these claims, the Division has an estimated obligation of \$6,400, recorded in the government-wide Statement of Net Assets, based on management's evaluation of the nature of such claims and consideration of historical loss experience for the respective types of action. Such claims will be recognized primarily as expenditures of the State Road Fund if, and when, they are approved for payment by the Legislature in accordance with legal statutes. Also included in claims are claims that have been settled in the court of claims and approved for payment through legislative action. These amounts total approximately \$561. During the normal course of operations, the Division may become subject to other litigation. Accordingly, no provision has been made in the financial statements for liabilities, if any, from such litigation.

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NOTE 8 - LONG-TERM OBLIGATIONS (Continued)

The Division's obligation for accrued vacation leave time includes leave time and related costs expected to be paid to employees in the future and are determined using wage levels in effect at the date the obligation is calculated. Also included in this amount is the Division's unfunded obligation of approximately \$4,604 arising in connection with legislation to fund portions of employee post retirement health insurance costs for retired employees. The Division has 428 former employees currently eligible for post employment health insurance. The Division's total expenditures for post-employment health benefits for the year ended June 30, 2003 were \$2,079. These liabilities are generally liquidated by the State Road Fund.

Upon retirement, an employee may apply unused sick leave or annual leave, or both to reduce their future insurance premiums paid to the West Virginia Public Employees Insurance Agency or to obtain a greater benefit under the West Virginia Public Employees Retirement System. These liabilities are generally liquidated by the State Road Fund.

NOTE 9 - RELATED PARTY TRANSACTIONS WITH THE STATE OF WEST VIRGINIA

The Division enters into certain transactions with various agencies of the State of West Virginia. The following summarizes the nature and terms of the most significant transactions:

- The Division leases from the Department of Administration substantially all of State Office Building No. 5 and a portion of State Office Building No. 3 which are owned by the State Building Commission. The Division may be released from its obligation only at the option of the lessor. The Division is obligated under these operating leases, which expire December 31, 2003 for rental payments of approximately \$1,796 annually. Management expects the leases to be renewed upon expiration.
- The Division's employees participate in various benefit plans offered by the State of West Virginia. Employer contributions to these plans are mandatory. During the year ended June 30, 2003, the Division incurred payroll related expenditures of approximately \$26,999 for employee health insurance benefits provided through the West Virginia Public Employees Insurance Agency and approximately \$16,663 in employer matching contributions to the State Public Retirement System.
- The Division is insured under the West Virginia Workers' Compensation Plan. During the year ended June 30, 2003 the Division paid approximately \$9,321 for employee workers' compensation benefits, which are paid into funds administered by the West Virginia Workers' Compensation Fund.
- The Division made payments to the Department of Military Affairs and Public Safety, Division of Public Safety for various services performed. These expenditures, which were authorized by the Legislature, amounted to approximately \$5,466 during the year ended June 30, 2003.

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NOTE 10 - COMMITMENTS AND CONTINGENCIES

The amount of unexpended balances of highway design and construction contracts entered into by the Division with various contractors approximated \$575,892 at June 30, 2003.

The Division participates in several federal programs which are subject to audit by the federal awarding agency. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures that may be disallowed by the federal awarding agency cannot be determined at this time. The Division expects such amounts, if any, to be immaterial to the financial position of the Division. The Division records these disallowed audit adjustments for questioned costs in the period the audit is finalized.

During the year ended June 30, 1989, the Division in-substance defeased Huntington Bridge Revenue Bonds dated January 1, 1965, by authorizing the West Virginia Municipal Bond Commission (MBC), the bond fiscal agent, to purchase U.S. government securities which will mature on dates to coincide with the remaining principal and interest payments. At June 30, 2003, \$1,905 of these bonds were outstanding and are considered defeased. Accordingly, the assets and liability for these defeased bonds have been excluded from the Division's financial statements.

NOTE 11 - RETIREMENT PLAN

**PLAN DESCRIPTION** - The Division contributes to the West Virginia Public Employees' Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan administered by the West Virginia Consolidated Public Retirement Board. Chapter 5, Article 10 of the West Virginia State Code assigns the authority to establish and amend benefit provisions to the PERS Board of Trustees. Employees who retire at or after age 55 and have completed 25 years of credited service are eligible for retirement benefits as established by State statute. Retirement benefits are payable monthly for life, in the form of a straight-line annuity equal to two percent of the employee's final average salary, multiplied by the number of years of the employee's credited service at the time of retirement. PERS also provides deferred retirement, early retirement, death, and disability benefits to plan members and beneficiaries. The West Virginia Consolidated Public Retirement Board issues a publicly available financial report that includes financial statements and required supplementary information for PERS. That report may be obtained by writing to the West Virginia Consolidated Public Retirement Board, 1900 Kanawha Boulevard East, Building Five, Charleston, West Virginia 25305 or by calling (304) 558-3570.

**FUNDING POLICY** - The PERS funding policy has been established by action of the State Legislature. State statute requires that plan participants contribute 4.5% of compensation. The current combined contribution rate is 14% of annual covered payroll, including the Division's contribution of 9.5% which is established by PERS. The Division's contributions to PERS for the years ended June 30, 2003, 2002, and 2001 were \$16,663, \$15,717, and \$15,275, respectively, equal to the required contributions for each year. Beginning July 1, 2003 the Division's contribution rate will increase to 10.5%.

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NOTE 12 - RISK MANAGEMENT

The Division is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; employee health and life coverage; and natural disasters. The State of West Virginia established the Board of Risk and Insurance Management (BRIM), the Public Employees Insurance Agency (PEIA), and the Workers' Compensation Fund (WCF) to account for and finance uninsured risks of losses for state agencies, institutions of higher education, and component units.

BRIM is a public entity risk pool that provides coverage for general, property, medical malpractice, and automobile liability. PEIA is also a public entity risk pool and provides coverage for employee and dependent health, life and prescription drug insurance. The WCF provides coverage for work related accidents and is considered an insurance enterprise fund. The Division retains the risk of loss on certain tort and contractor claims in excess of the amount insured or covered by BRIM's insurance carrier. Other than the amounts disclosed in Note 9, amounts of settlements have not exceeded insurance coverage in the past three years. The Division has evaluated this potential risk of loss as discussed in Note 9.

Through its participation in the PEIA and WCF, the Division has obtained health coverage and coverage for job related injuries for its employees. In exchange for payment of premiums to PEIA and WCF, the Division has transferred its risks related to health coverage and job related injuries of employees. These entities issue publicly available financial reports that include financial statements and required supplementary information. Those reports may be obtained by writing to these specific entities.

NOTE 13 - RESTATEMENT OF PRIOR YEAR AMOUNTS

During the current year it was determined that an undercapitalization of infrastructure assets had occurred in the initial implementation of the provisions of GASB Statement 34 *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. Certain projects that met the capitalization criteria were excluded from Work in Process and other projects that were completed were not properly capitalized into infrastructure. This undercapitalization of infrastructure assets had no impact on the fund or budgetary comparison financial statements for the year ended June 30, 2002. The following summarizes the impact of this undercapitalization of infrastructure assets on the government-wide financial statements:

	<u>As Previously Reported</u>	<u>Adjustment</u>	<u>Restated</u>
Total capital assets	\$5,658,540	\$320,996	\$5,979,536
Total assets	\$6,020,546	\$320,996	\$6,341,542
Net assets - investment in capital assets, net of debt	\$5,198,392	\$320,996	\$5,519,388
Total net assets	\$5,283,667	\$320,996	\$5,604,663
Total expenses	\$1,074,962	\$(268,740)	\$806,222
Change in net assets	\$(41,693)	\$268,740	\$227,047

COMPLIANCE AND INTERNAL CONTROL REPORT

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON  
AN AUDIT OF GENERAL PURPOSE FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE  
WITH *GOVERNMENT AUDITING STANDARDS*

Joint Committee on Government and Finance  
West Virginia Legislature

We have audited the financial statements of the West Virginia Department of Transportation, Division of Highways as of and for the year ended June 30, 2003, and have issued our report thereon dated October 31, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the West Virginia Department of Transportation, Division of Highways' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings as items 2003-2 through 2003-5. Additionally, we noted certain immaterial instances of noncompliance that we have reported to management of the West Virginia Department of Transportation, Division of Highways, and the Joint Committee on Government and Finance in a separate letter dated October 31, 2003.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the West Virginia Department of Transportation, Division of Highways' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the West Virginia Department of Transportation, Division of Highways' ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying schedule of findings as items 2003-1 through 2003-6.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above is a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to management of the West Virginia Department of Transportation, Division of Highways, and the Joint Committee on Government and Finance in a separate letter dated October 31, 2003.

This report is intended solely for the information of the West Virginia Legislature, the Division's management, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*Suttles & Stalnaker, PLLC*

October 31, 2003



WEST VIRGINIA DEPARTMENT OF TRANSPORTATION,  
DIVISION OF HIGHWAYS  
SCHEDULE OF FINDINGS  
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2003-1

Information Systems Controls

Criteria:

The management of the Division is responsible for establishing and maintaining adequate information systems internal controls. Furthermore, an integral part of an entity's internal control structure is the effective segregation of duties, which involves assigning responsibilities for authorizing transactions, recording transactions and maintaining custody of assets to different individuals, thus reducing the risk of irregularities or defalcations occurring and not being detected.

Condition:

The Division operates a wide variety of computer applications, many of which affect federal and state programs' data. During our review of the information systems controls we noted the following:

- There are no formal policies and procedures for review and monitoring of the user account access maintenance. (Also noted in prior year)

Specifically, there are no policies and procedures in place for the review of user account access maintenance in the REMIS system. When user accounts are modified and access rights are changed, it is important to have changes reviewed by a third party to preclude an accidental or intentional inappropriate change.

- There are no formal policies and procedures for review and monitoring of various information system security reports such as the "failed access report." (Also noted in prior year)

Specifically, the Information Services and Communications Department (IS&C) of West Virginia creates a report of failed login attempts; however, there is no review of this report by the Division personnel. A report of failed logins provides information and clues that there may be unauthorized attempts being made at access into the network. Failure to review this report increases the possibility of undetected intrusion attempts.

- Through IS&C, the Division did have a web intrusion vulnerability test conducted during the period of review. However, there are no policies and procedures in place for conducting periodic intrusion vulnerability testing of the various computer systems maintained by the Division. (Also noted in prior year)

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2003-1

Information Systems Controls (Continued)

Condition:  
(Continued)

Specifically, the intrusion vulnerability test report presentation provided to us during our review had no date of testing. In addition, the presentation showed several severe security vulnerabilities. A second test presentation was provided, which showed many of the vulnerabilities patched, but some still active. No formal test report was available for our review. All testing was performed under the responsibility of the IS&C and was not under the control of the Division. Furthermore, there was no Division or IS&C policy requiring periodic vulnerability testing evident. Also, while it was disclosed that network monitoring is performed, there was no knowledge of what level of intrusion attempt would initiate disclosure to the Division if detected by IS&C. Given the continuous development of intrusion methods, it is very important to have regular testing of known vulnerabilities. Information from the test reports provides the ability to modify and patch the known security weaknesses in systems. Knowledge of the level of intrusion attempt that would initiate notification to the Division provides better assurance that the parties responsible for monitoring intrusion detection systems will provide appropriate protection at appropriate times.

Programmers in the Division's Information Services Department have access to production programs in the REMIS system. This access grants the Division's Information Services Department personnel the same rights as a business user of the application, which allows them access to data and transaction authority.

Context:

Information systems controls potentially can affect all federal and state programs and are critical to the daily operations of the Division.

Cause:

Policies and procedures have not been adequately updated and information system controls have not been monitored by the Division.

Effect:

Unauthorized access to critical information systems may occur and not be detected.

Recommendation:

We recommend that the Division strengthen their policies and procedures related to information systems controls and ensure that controls are operating as designed. Specifically, we recommend that an individual other than those responsible for adding and making changes to user rights review changes made to user access in the REMIS system. The Division should also consider requiring the individuals who have responsibility for certain system access areas such as payroll, accounts receivable, etc., to periodically review for accuracy the listing of individuals who have access to those systems. These processes should be documented in the policies and procedures of the Division.

Also, we recommend that all intrusion detection reports available be reviewed regularly by authorized personnel. We further recommend that an action plan and procedure be implemented outlining the steps to be taken when an intrusion is detected.

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Information Systems Controls (Continued)

Recommendation:  
(Continued)

Furthermore, the Division should work with IS&C to ensure that periodic intrusion vulnerability testing is conducted for all significant systems utilized by the Division. Also, we recommend that the Division remove programmer access from production applications and develop policies and procedures regarding programmer access. If this access is necessary, mitigating controls such as monitoring of programmer access and activities within the production application should be performed and documented. In addition, the internal audit group of the Division should consider designing audit procedures for the monitoring and review of information system controls.

Management Response:

- *Agree. In the prior year's response we agreed to develop these policies and procedures in conjunction with management. We recommend the following policies and procedures and will include them in the Division's procedures upon approval.*
  1. *Assignment of review of users with rights to certain system access areas, such as payroll, accounts receivable, etc., will be to the manager responsible for the system.*
    - a. *Monthly, Information Services will provide a report of user accounts with access to a specific system to the manager responsible for that system. (For example, a report of all users with access to the Personnel System will be sent to the Human Resources Division Director.)*
    - b. *The manager responsible for the system will review the system user access report to identify inaccuracies.*
    - c. *The manager responsible for the system will report inaccuracies to the Director of Information Services and to other management as appropriate.*
  2. *Information Services Division will continue the current practice of sending a monthly user access report to the manager of each organization to confirm that the access privileges for users of their own organization are appropriate.*
- *Agree. In the prior year's response we have been reluctant to commit scarce resources to this task with such a low return on investment. However, we now recommend the following policies and procedures and will include them in the Division's procedures upon approval.*
  1. *Information Services Division will review the Failed Access Report each workday to identify patterns of violations (over successive days) that may indicate unauthorized access attempts.*
  2. *Information Services will notify the user's management (Division Directors and District Comptrollers) and Transportation Auditing Division of the suspected access violation events so that they may investigate the user's actions and intent.*
  3. *Results of the investigation will be reported in a timely manner to the Director of Information Services Division and to other management as appropriate.*

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Information Systems Controls (Continued)

4. *Appropriate corrective actions will be taken as a result of the investigation and consultation with appropriate management.*

- *Agree. Access from the DOT network to the Internet is through the State's backbone, exclusively. Therefore, the intrusion detection services of IS&C and Trust Wave, the contract vendor, provide us with comprehensive coverage. This service has performed well and we have been alerted to some events to which we have taken immediate and appropriate action.*

*The results of the two vulnerability tests have not revealed any unknown or unacceptable security vulnerabilities and no security patching was required. The openings in our network that were identified in these vulnerability tests were: internet/e-mail, which we must have to conduct business and that we protect with a firewall, Websense and with F-Secure and Antigen antivirus programs; FTP (File Transfer Protocol) which is user identified and authenticated by password for contractor's and others; and VPN (Virtual Private Network) which permits controlled, user identified and password authenticated access for employees and some of our IT contractors.*

*We have recommended to IS&C that statewide policies are needed for their intrusion detection program. These policies should include the intrusion reporting parameters and they should also include intrusion response policies and procedures. Also, we have recommended to IS&C that vulnerability testing be conducted at least twice per year and that formal reports be provided.*

*We are committed to continuing to work with IS&C on the intrusion detection and vulnerability testing policies and procedures issues. Also, we will develop DOT intrusion response policies and procedures, once the statewide policies are issued.*

- *Agree. Change Management Control is the issue here with the fundamental control being a separation of duties that would require splitting our staff and responsibilities into development groups and production groups. We acknowledge this in principle, but maintain that we have an insufficient number of personnel to support this.*

*We maintain control through supervisor monitoring and end product review prior to implementation. Also, we solicit review and approval by the manager responsible for the specific system for significant programs and changes.*

*However, we will review our operations and practices against the standards of Change Management. Following this review, we will develop a proposal, including costs, and present this proposal to the Business Manager for decision-making. Upon receipt of a decision, we will develop the approved plan including policies and procedures regarding programmer access as well as mitigating controls and required documentation.*

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2003-2

Accounts Receivable Collection and Financial Reporting

Criteria:

Article V of the Constitution of West Virginia states in part that, "the legislative, executive and judicial departments shall be separate and distinct, so that neither shall exercise the powers properly belonging to either of the others." Furthermore, Article 10, Section 6 of the Constitution of West Virginia states in part that, "credit of the state shall not be granted to, or in aid of any county, city, township, corporation or person; nor shall the state ever assume, or become responsible for the debts or liabilities of any county, city, township, corporation or person." Furthermore, the Division's accounts receivable policies and procedures state that entities with past due balances will have credit discontinued until the account is brought current.

Condition:

We noted that management of the Division has extended credit to other entities, including State agencies and political subdivisions that have accounts receivable balances that are past due. Thus, the Division significantly decreases their ability to collect these balances through the regular collection process. (Also noted in prior year)

Context:

The total allowance for doubtful accounts as of June 30, 2003 was approximately \$2.3 million. The total accounts receivable for this category of transactions as of June 30, 2003 was approximately \$8.6 million.

Cause:

Management of the Division has extended credit to entities, including other State agencies and political subdivisions of the State that have accounts receivable balances that are past due.

Effect:

The extension of credit to other State agencies and political subdivisions could be construed as the Division appropriating funds, thus usurping the constitutional authority the legislature.

Recommendation:

We recommend that the Division suspend the extension of credit to entities, including other State agencies and political subdivisions with past due balances until the account is brought current. Also, we recommend that the Division evaluate the requirements of West Virginia State Code and determine if revisions to and/or exclusions to the Code should be considered.

Management Response:

*The Division of Highways agrees with the recommendation that a policy be developed to analyze the accounts for Accounts Receivable. We will incorporate the policy dealing with the collections into the existing collection policy for the Accounts Receivable Section. We also offer the following comments. Please remember the state suffered many disasters the past year and DOH may have extended credit to counties, cities or towns affected. But these will be reviewed and analyzed during the current year.*

1. *The Division of Highways does cease credit extension for entities that have past due balances. For hauling permit and escort services accounts through our Maintenance Division, and our "SS" accounts (bid letting and specs) no further charges are allowed until the balance is paid in full. Trucks often have to wait at the state line because we will not issue permits or provide escorts on an overdue account. When entities that have leases with Property Management for sign (logo) rental or property rentals become delinquent, they are notified that their lease will be cancelled or their signs removed.*

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Accounts Receivable Collection and Financial Reporting (Continued)

2. *In the case of governmental entities, the situation is more complicated. The Division aggressively employs every legal recourse available to collect debts from entities such as County Commissions, Public Service Divisions, Towns, School Boards, Prisons, and State Agencies. We have a record of taking many of these entities to the Court of Claims for collection, where we have been overwhelmingly successful. However, this is often a more complex situation than can be dealt with by a simple refusal of services. For example, we have had Emergency Services Organizations with an outstanding balance need gasoline for an ambulance or a school board for its buses. Often in rural areas we are the only source for gasoline in emergency situations. During the past several years the number of governmental entities obtaining gasoline from the Division of Highways has significantly decreased. It has been our goal to eliminate this service completely, but emergency situations arise where this is impossible. We receive calls from members of the legislature requesting the Division's services for their constituency in dire circumstances such as water hauling during a drought or assistance from flood damage. Some of these situations are on an emergency status from the Governor's Office and some are not. The Division of Highways asserts that government must provide for its citizens particularly in exigent circumstances. The Division has responded to these requests with this premise rather than a strictly financial one. The Division seeks guidance from the Legislature for handling matters such as these and requests for services to governmental entities from the Governor's Office on a non-emergency basis to entities indebted to the Division. The Division is currently carrying balances for many government entities for water emergency services.*
3. *The Division does not agree that the extension of credit to entities with outstanding balances "significantly decreases their ability to collect these balances through the regular collection process". There are two applicable time periods for the collection of debts. We have 2 years to collect non-contractual debts and 10 years to collect debts incurred by contract. The Statute of Limitations begins to run when the debt is incurred or the contract is signed. Therefore, subsequent debts have no effect on collecting a prior debt that has a different Statute of Limitations. During the applicable time period Accounts Receivable, the Claims Division, and ultimately the Legal Division work systematically to obtain payment. Prior to the Statute of Limitations expiring, the debt is referred to the Legal Division where a determination is made whether to file a lawsuit. Many factors are considered primarily being if the entity has sufficient funds or assets to satisfy a judgment. If it appears feasible to file a lawsuit, a case is filed in Circuit Court or a claim in the Court of Claims. When the Division receives a judgment, every means available to execute the judgment is pursued.*

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2003-3	Independent Engineer's Cost Estimate
Criteria:	Section 157-1-7.7b of the Code of State Rules requires the director of the division initiating the request for service to be responsible for preparing an independent engineer's cost estimate prior to the receipt of the fee proposal from the consultant.
Condition:	As noted in the prior year, we noted several instances in which the engineer's cost estimate was not prepared by the Division until after the consultant's price proposal was received.
Context:	Total expenditures for architectural and engineering services were approximately \$81.9 million for the year ended June 30, 2003.
Cause:	Due to staff and time limitations, the Division has been unable to prepare the independent engineer's cost estimate prior to receipt of the fee proposal from the consultant.
Effect:	The Division is in noncompliance with the Code of State Rules and cost estimates prepared by the Division risk being influenced by submitted proposals.
Recommendation:	We recommend that the Division devote the necessary resources to ensure that the Code of State Rules and its policies and procedures are followed and cost estimates are prepared in a timely manner.
Management Response:	<i>WVDOH has undertaken various actions to address this issue, including devoting additional resources to preparation of the independent engineer's cost estimate. The Division feels that the previous actions undertaken, and the additional resources taken this past year will ensure that future cost estimates will be prepared in a timely manner.</i>

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2003-4

Procurement of Architectural and Engineering Services

Criteria:

Chapter 5A, Article 8, Section 9 of the West Virginia Code states in part that: "The head of each agency shall make and maintain records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures and essential transactions of the agency designed to furnish information to protect the legal and financial rights of the state and of persons directly affected by the agency's activities." Section 157-1-7.3n of the Code of State Rules states in part that: "A written expression of interest made by the consultant indicating his desire to perform a particular project, task or service. This shall include, as a minimum, a current qualification questionnaire, location of where work would be performed, cost accounting information statement..." Further, Section 157-1-7.16 states: "Record Keeping. Unless otherwise noted, all documentation under this procedure will be retained on file at the Division of Highways and would be available for review by the FHWA."

Condition:

We noted the following during our review of documentation related to the procurement of architectural and engineering services:

- The Consulting Services Section of the Engineering Division did not have a Consultant Confidential Qualification Questionnaire and/or Consultant Cost Accounting Information Statement on file for seven of the projects tested. (Also noted in prior year)
- For several of the projects reviewed, the reasons for why a vendor was selected and the interviews of consultants were not documented. (Also noted in prior year)
- The Consulting Services Section of the Engineering Division does not document that the consultant; 1) is registered and is in good standing with the State Tax Department and Bureau of Employment Programs; and 2) that at least one of the key consultants anticipated to be used on the project is registered and is in good standing with the Board of Registration for Professional Engineers.

Context:

Total expenditures for architectural and engineering services were \$81.9 million for the year ended June 30, 2003.

Cause:

The Division was unable to locate some of the documentation and policies and procedures of the Division do not clearly specify the documentation which should be maintained.

Effect:

The Division was unable to provide supporting documentation related to compliance with the West Virginia State Code.

Recommendation:

We recommend that the Division strengthen their policies and procedures regarding required documentation for the procurement of architectural and engineering services.

Management Response:

- *WVDOH will retain the necessary information in our project files to show that a Consultant Confidential Qualification Questionnaire and Consultant Cost Accounting Information Statement was on file during the year that the consultants were selected.*



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Procurement of Architectural and Engineering Services (Continued)

- *WVDOH disagrees with this part of the finding. The Division feels that the necessary documentation is contained in the files. The memo from the pre-selection committee states that everyone on the short-list has been interviewed by at least one member of the pre-selection committee. The pre-selection committee states the reasons why the firms were selected for the short-list, and that they have met the selection criteria. All firms on the short list are considered to be equal and the selection committee is required only to select the firm to provide the required services, and to select a 1<sup>st</sup> and 2<sup>nd</sup> alternate if an agreement can not be reached with the selected firm.*
- *WVDOH will document that all the firms on the short-list are in good standing with the State Tax Department and Bureau of Employment Programs, and that they have at least one WV Registered Professional Engineer in their firm that will supervise all engineering work. This will be reviewed again at the time a contract is executed with the engineering firm.*

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2003-5

Evaluation of Consultant's Work

Criteria:

Chapter 5A, Article 8, Section 9 of the West Virginia Code states in part that: "The head of each agency shall make and maintain records containing adequate and proper documentation of the organization, functions, policies, decisions, procedures and essential transactions of the agency designed to furnish information to protect the legal and financial rights of the state and of persons directly affected by the agency's activities." Further, Section 157-1-7.10 of the Code of State Rules states that: "Upon completion or performance termination of the consultant's work, the responsible Division will prepare a report recording its evaluation of the consultant's efforts. A copy shall be sent to the consultant for review and comment and any written comments received shall be attached to the final report. All consultants with active contracts shall be evaluated in March of each year on each active project. On contracts where the final product has been accepted by the Division but the final invoice has not been paid, the consultant will not need to be evaluated..."

Condition:

We noted the following during our review of the Division's evaluation of consultants' work:

- The March annual consultant evaluations could not be located for seven of the active projects reviewed. (Also noted in prior year)
- For one project reviewed, there were no progress notes, even though a "Notice to Proceed" was given to the consultant.

Context:

Total expenditures for architectural and engineering services were \$81.9 million for the year ended June 30, 2003.

Cause:

The Division indicated that evaluations are performed at the preliminary field review, final field review, and final grade review and that these evaluations may be retained by the project manager in the project files. As of the date of fieldwork, these evaluations had not been provided.

Effect:

The Division was unable to provide supporting documentation related to compliance with the West Virginia State Code.

Recommendation:

We recommend that the Division strengthen their policies and procedures regarding required documentation for the evaluation of consultants.

Management Response:

*All evaluations of consultant work will be placed in the files in the Consultant Services Section of the Engineering Division. The WVDOH has undertaken new efforts to prepare consultant evaluations at each major milestone of the project. The Division will amend the WVDOH procedures to reflect this new procedure for consultant evaluations.*

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2003-6 Financial Reporting - Infrastructure (*Internal Control*)

- Criteria: The management of the Division is responsible for establishing and maintaining adequate controls that are sufficient to ensure accounting for capital assets and related depreciation in accordance with Government Auditing Standards Board Statement No. 34 *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* (GASB 34).
- Condition: GASB 34 was implemented for the year ended June 30, 2002, and required a number of significant changes in reporting, including the requirement to present a government-wide statement of net assets and a government-wide statement of activities in addition to the more traditional fund financial statements. This also required the Division to record infrastructure (roads, bridges, etc.) and the related accumulated depreciation as of June 30, 2003 on the government-wide statement of net assets, and to reflect the effects of this on the government-wide statement of activities. This significant change in reporting presentation required significant resources of the Division to develop an estimate for the infrastructure asset balance and the related accumulated depreciation at June 30, 2002, and to reflect the activity of the 2002 fiscal year. During the development of the information as of and for the year ended June 30, 2003, it was discovered that information extracted from the Division's information systems utilized for the estimate was not correct. As a result, the beginning net asset balance on the government-wide statement of net assets was restated, and Management's Discussion and Analysis was modified accordingly.
- Context: The total restatement to the beginning net asset balance as reported on the Statement of Net Assets was approximately \$321 million out of total net assets of approximately \$6 billion.
- Cause: An undercapitalization of infrastructure assets occurred during the initial implementation of the provisions of GASB 34 and certain projects that met the capitalization criteria were excluded from the work-in-process and other projects that were completed were not properly capitalized into infrastructure.
- Effect: Information previously reported in the government-wide financial statements were restated. There was no effect on the fund or budgetary comparison financial statements of the Division.
- Recommendation: We recommend that the Division continue to develop policies and procedures to ensure that data extracted from the information systems of the Division is accurate and complete. The procedures should include providing for adequate testing of the data extraction runs to minimize the risk of errors in complying with the requirements of GASB 34.

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Financial Reporting - Infrastructure (*Internal Control*) (Continued)

Management Response:

*The Division has revised the process used to develop infrastructure data and is in the process of updating its infrastructure policy to include the provision for adequate testing of generated data. The reports used to compile the infrastructure figures have been tested and will continue to be tested in the future. In the prior year, we used two reports to obtain the financial information for selected projects, one for open authorizations and one for closed authorizations. Neither of these reports showed all of the authorizations for all projects that met the capitalization threshold. It was determined that in the future years these reports will be modified to include all authorizations for projects that meet the capitalization threshold. In order to determine if all projects meeting the capitalization threshold were properly identified and that amounts capitalized in the current year as work in process were correct, management obtained reports from both the authorization system and the project tracking system and conducted procedures to ensure that all projects that met the capitalization policy were properly identified, all authorizations related to those projects were captured, and that the amounts determined were consistent among the two systems.*

*Management is confident that the new methods and documentation provide adequate assurance that the data will be accurate in the future. In addition, the documentation format has been revised to facilitate management review and audit.*